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No. 600

In the Supreme Court of the United States

OCTOBER TERM, 1961

ARD E. RICHARDSON, JR., ET AL., PETITIONERS

v.

THE UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The opinion of the District Court (Pet. 21–26) is reported at 177 F. Supp. 394. The opinion of the Court of Appeals (Pet. 28–36) is reported at 294 F. 2d 593.

JURISDICTION

The judgment of the Court of Appeals was entered on September 19, 1961. (Pet. 36.) The petition for a writ of certiorari was filed on December 11, 1961. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether interest that had accrued but not been paid to a cash basis taxpayer prior to his death can constitutionally be taxed as income to the person or estate acquiring the right to receive the amount from the decedent or by reason of the decedent's death.

STATUTE INVOLVED

Internal Revenue Code of 1939:

> SEC. 126. [as added by Sec. 134(c) of the Revenue Act of 1942, c. 619, 56 Stat. 798]. INCOME IN RESPECT OF DECEDENTS.
>
> (a) *Inclusion in Gross Income*—
>
> (1) *General rule.*—The amount of all items of gross income in respect of a decedent which are not properly includible in respect of the taxable period in which falls the date of his death or a prior period shall be included in the gross income, for the taxable year when received, of:
>
> (A) the estate of the decedent, if the right to receive the amount is acquired by the decedent's estate from the decedent;
>
> (B) the person who, by reason of the death of the decedent, acquires the right to receive the amount, if the right to receive the amount is not acquired by the decedent's estate from the decedent; or
>
> (C) the person who acquires from the decedent the right to receive the amount by bequest, devise, or inheritance, if the amount is received after a distribution by the decedent's estate of such right.
>
> * * * * *
>
> (3) *Character of income determined by reference to decedent.*—The right, described in

paragraph (1), to receive an amount shall be treated, in the hands of the estate of the decedent or any person who acquired such right by reason of the death of the decedent, or by bequest, devise, or inheritance from the decedent, as if it had been acquired by the estate or such person in the transaction by which the decedent acquired such right; and the amount includible in gross income under paragraph (1) or (2) shall be considered in the hands of the estate or such person to have the character which it would have had in the hands of the decedent if the decedent had lived and received such amount.

* * * * *

(c) *Deduction for Estate Tax.*—

(1) *Allowance of deduction.*—A person who includes an amount in gross income under subsection (a) shall be allowed, for the same taxable year, as a deduction an amount which bears the same ratio to the estate tax attributable to the net value for estate tax purposes of all the items described in subsection (a)(1) as the value for estate tax purposes of the items of gross income or portions thereof in respect of which such person included the amount in gross income (or the amount included in gross income, whichever is lower) bears to the value for estate tax purposes of all the items described in subsection (a)(1).

* * * * *

(26 U.S.C. 1952 ed., Sec. 126.)

STATEMENT

This action involves the federal income tax liability of the taxpayers for the calendar year 1948.

The facts, all of which were stipulated (R. 12a–21a),[1] are as follows:

Ard E. Richardson (the decedent), a resident of Lansing, Michigan, died testate on September 21, 1945, leaving as his heirs, his widow, Irene B. Richardson,[2] and his son, Ard E. Richardson, Jr. (R. 14a; Pet. 29.)

Included in the assets of the decedent's estate were seven promissory notes payable by the E. Richardson Corporation to the decedent. The notes were included in the decedent's gross estate for federal estate tax purposes at their fair market value, namely, a total principal amount of $139,000 plus accrued interest to September 21, 1945 (the date of the decedent's death), in the amount of $411,593.33. (R. 14a–15a; Pet. 29.)

On February 16, 1948, the probate court entered an order approving distribution of the promissory notes plus total accrued interest. The distribution was on the basis of one-quarter to the widow (in accordance with her election to take her statutory share of the decedent's estate) and three-quarters to the son. Thereafter, on June 11, 1948, the E. Richardson Corporation paid the principal and ac-

[1] "R." refers to the appendix to the petitioners' brief in the Sixth Circuit.

[2] Irene B. Richardson later married Peter C. Treleaven and became Irene B. Treleaven. Mildred G. Richardson, wife of the son, and Peter C. Treleaven are parties to this proceeding because they filed joint returns with their spouses for the year 1948. All references to the "taxpayers" are to the son and his wife and to the estate of the widow and Peter C. Treleaven.

crued interest then owing on the notes. (R. 14a, 15a–16a; Pet. 29–30.)

The son and the widow, with their spouses, in joint individual income tax returns for the year 1948, included as interest income that portion of the interest received by them which had accrued as of the date of decedent's death and claimed a deduction under Section 126(c) of the 1939 Code for federal estate taxes paid thereon by the decedent's estate. (R. 16a–17a; Pet. 30.)

Claims for refund were filed by the taxpayers. They contended, *inter alia,* that the interest which had accrued up to the date of decedent's death was excludible from gross income on the ground that Section 126(a) of the 1939 Code unconstitutionally levies a tax on capital without that apportionment required by Article 1, Section 2, Clause 3 and Article 1, Section 9, Clause 4. The refund claims based on this contention were rejected by statutory notice of disallowance. (R. 17a–19a; Pet. 30–31.) Timely suit for refund was filed by the taxpayers in the District Court. (R. 19a.) The trial court entered judgment for the United States, holding Section 126(a) of the 1939 Code constitutional. (R. 22a–29a; Pet. 21–27.) The Court of Appeals for the Sixth Circuit affirmed.

ARGUMENT

1. Section 126(a)(1) of the 1939 Internal Revenue Code, *supra,* p. 2, provides that "all items of gross income in respect of a decedent" not properly includible in the last taxable period of the decedent shall be included when received in the gross income

of his estate or of the person who acquires the right to such amount. Subsection (a)(3) provides that a subsection (a)(1) item shall be considered, in the hands of the estate or the heir, to have the character which it would have had in the hands of the decedent if he had lived and received it.

The accrued interest in the instant case, which would have constituted income to decedent had he lived, was not taxable to him during his lifetime because he reported income on the cash receipts basis. Nor was there any statutory warrant for considering it as includible in his last taxable period. Thus, it was clearly Section 126(a) income, concededly taxable to petitioners if that statute is constitutional. (Pet. 32.)

Taxpayers, however, contend that Section 126(a) provides for a direct tax on capital, without apportionment, and is therefore unconstitutional. Their argument rests on the premise that the interest here involved was converted into capital by the single fact of decedent's death. This premise, which is asserted without any support except for an analogy to state probate law, ignores the fact that Congress may, consistent with proper accounting and economic concepts, treat the collection of interest as necessarily a realization of income either to the decedent or his estate. Since it was admittedly not a realization to the cash basis decedent, it could properly be considered income to the estate or heir when received. See, *Estate of Putnam* v. *Commissioner*, 324 U.S. 393, 397, fn. 4; *Taft* v. *Bowers*, 278 U.S. 470, 481–482. As this Court observed in *Estate of Putnam*—in distinguishing the

situation in that case from *Vanderbilt* v. *Commissioner*, 11 B.T.A. 291, and *Nichols* v. *United States*, 64 C. Cls. 241, both of which are cited by taxpayers herein (Pet. 6, 9)—"If [dividends] * * * are income to the decedent, they cannot be income also to the estate. If they are not income to the decedent, they are income to the estate."

In *Taft* v. *Bowers*, *supra*, this Court rejected a rationale similar to that which the taxpayers advance here. In 1921 and 1922 a donor gave to his daughter shares of stock which had appreciated in value over their cost. The daughter, who sold the stock during 1923 at a still higher price, was required by the collector to pay an income tax on the difference between the cost to the donor and the price at which she sold the stock. She contended that she was liable for tax only on the increase in value of the stock while she held it and that any tax levied against her on the appreciation in its value prior to the gift was an unconstitutional tax on capital, since the stock was capital in her hands to the extent of its value at the time of the gift. This Court concluded that she was required, in computing gain on the sale, to take the donor's basis, stating (p. 483): "Congress had power to require that for purposes of taxation the donee should accept the position of the donor in respect of the thing received." In like manner, in the instant case, the taxpayers took the position of the decedent in respect of the accrued interest and it was income to them upon receipt, as it would have been to the decedent had he lived to receive it.

Finally, the lower courts have repeatedly held that the subject of the tax imposed by Section 126(a) is income. *O'Daniel's Estate* v. *Commissioner,* 173 F. 2d 966 (C.A. 2d); *Dixon* v. *United States,* 96 F. Supp. 986 (E.D. Ky.), affirmed, 192 F. 2d 82 (C.A. 6th); *Commissioner* v. *Linde,* 213 F. 2d 1 (C.A. 9th); *Estate of Basch* v. *Commissioner,* 9 T.C. 627. In *Estate of Basch,* the Tax Court, adverting to this Court's decision in *Taft* v. *Bowers, supra,* expressly considered and upheld the constitutionality of Section 126(a).

The cases cited by the taxpayers (Pet. 8–9) [1] are distinguishable. They hold only that amounts originally received as income in respect of a decedent may, when later distributed by the estate, be treated as capital distributions for the different purposes of determining deductions under Section 162 of the 1939 Code. Of course, what is ultimately distributed as capital need not have been received as such.

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[1] *Estate of Huesman* v. *Commissioner,* 16 T.C. 656, affirmed on other grounds, 208 F. 2d 133 (C.A. 9th); *Linde* v. *Commissioner,* 17 T.C. 584, reversed on other grounds, 213 F. 2d 1 (C.A. 9th); *Estate of Clymer* v. *Commissioner,* decided July 30, 1954 (1954 P–H T.C. Memorandum Decisions, par. 54,218), reversed, 221 F. 2d 680 (C.A. 3d); *Estate of Carruth* v. *Commissioner,* 28 T.C. 871; *Midland National Bank of Billings* v. *United States,* 168 F. Supp. 736 (D. Mont.).

CONCLUSION

The decision below is correct. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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